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# THE ORGANIZATION AND MANAGEMENT OF A BOND HOUSE

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Bond house is the name used to denominate a partnership or corporation formed or organized to buy and sell evidences of municipal or corporation debt. All bond houses are also banking houses in that they advance money to municipalities and public corporations, and their business is distinguished chiefly from other banking in that they do not transact commercial business. In this country the name bond house, by custom, has come to apply to those houses which endeavor to sell bonds strictly on the investment value by advertisement, circular letters and personal solicitation, as distinguished from banking houses, which accept deposits and deal in other securities as well as bonds; and from brokerage houses, which deal in bonds but on a commission basis only.

The organization of a bond house comprises: First, a buying department; second, a selling department, and, third, a financial department. The duties of these departments may be analyzed under these various heads.

## *The Buying Department*

The first duty of the buying department is to examine into the safety of such investments as may come into the market for sale. In the case of corporation bonds this will necessitate critical and careful examination of the assets, physical value, franchises and rights, past and present earning power and management of the corporation desiring to borrow. With the loans of municipalities, a close inquiry must be made of the valuation of the property, the extent of the existing debt, character of the officials and general reputation of the borrowing communities. Once the decision is made that the security offered is ample, and that the obligation will be secure beyond question, the matter of price requires consideration.

Since the limitations of the business the bond house can do are

dependent on its ability to sell, and to borrow pending sale, the matter of price becomes one for consultation with the other departments. The selling department can best judge of the ease with which the bonds may be sold, and the probable figure at which sales may be made; the financial department can best determine the desirability of the bonds as collateral.

If all of these questions are satisfactorily answered, it remains for the buying department to make the purchase at the best price possible, but not above such a price as will secure, in all probability, a fair profit. All purchases are made on the condition that the legality of the issue shall first be approved by the attorney for the bond house, and for this purpose certified copies of all papers precedent to the issue must be prepared. In many cases the bonds are issued under the direction and advice of the attorney for the purchasers.

When the bonds are prepared, it will then become the duty of the buying department to examine them for signature, certifications and seals, and to see that a proper delivery is made, which includes payment for the bonds to the proper party. The purchase now being made, the bonds are turned over to the financial department.

Recapitulating the duties of the buying department, they may be stated as follows:

First. To buy only such bonds as are safe.

Second. To see that the bonds have been issued legally.

Third. To buy as cheaply as possible.

All other duties of the buying department are tributary to these.

The work of the buying department as considered up to this time consists of the buying of new and original issues; but more often it is called upon to purchase blocks of bonds of old issues on which there is a known market. In order that the buying department may have the necessary information on file, it is the custom in all properly constituted bond houses to maintain a library of information, or, as it is more often called, a statistical file. This library of information will contain the well-known manuals of information in regard to railroads and corporations extending over a number of years, files of the current financial publications, the supplements of the *Financial Chronicle*, envelopes containing newspaper clippings concerning the various corporations, which files should also contain an account of any personal observations of the properties which it

may be possible to make. As to these last observations the bond house should encourage its employees to put into writing any personal observations they may make or any interesting gossip they may hear of the various corporations. No piece of information is of too little value to keep. The library of information will also contain the books, supplements and publications relative to municipalities, with complete records of past municipal sales and prices.

The circular offerings of other houses should also be kept carefully, and reference indices to the various offerings should be placed in the information file of each corporation or municipality. The objects of the library of information are apparent, briefly they may be stated to be:

First. To enable the buying department to judge quickly of the security offered.

Second. To offer a complete record of the prices at which the security has sold.

Third. To locate possible buyers or sellers of the bond in question.

*It is an axiom of the bond business that a bond well bought is already sold.*

### *The Selling Department*

Since bonds are bought usually at wholesale and sold at retail, the selling department will use more employees than the buying department. The first duty of the buying department is to see that the funds of the bond house are safely invested; the first duty of the selling department is to develop its ability to sell, as on that ability the growth of the business depends.

The selling department should consist of a manager, office salesmen, and outside salesmen, with the necessary assistants. The manager should be a man who has not only a wide knowledge of securities in general, but who is full of market information, and who will know instinctively in what market a security will be well received. It will also be his duty to regulate the price at which the security should be offered, and direct the efforts of the salesmen. In large houses more than one manager may be needed, and such managers' duties may be divided either on the line of the classes of bonds, or as to the territory where sales are made. The manager must always be in close touch with his salesmen, and upon taking

up a new offering should talk over the issue exhaustively in order that the salesman may not only understand the desirability of the security, the reason why his house has bought it and why it recommends it; but also that he may become enthusiastic about it and go out on his business with the innate feeling that he can sell the security.

The office salesmen may be divided into two classes, the men who meet and talk with clients who come into the office, and the men who prepare circulars and letters. Salesmen of every class must be men of more than usual intelligence and must know bonds and the bond business; but it is especially important that the office salesmen should be men of pleasing personality, with quick memories of people and events. The men who prepare circulars and write letters are the men behind the guns. Letters must be direct, forceful and in good English. In bond literature unnecessary prolixity is a sin. As a rule, more bond buyers know a house through its circulars and letters than in any other way. Therefore on the intelligence, directness and business-like form of these communications, the opinion of many possible customers will be formed.

The outside salesmen are composed of city men and traveling men, and it is their duty to sell bonds by personal solicitation. Their work is more difficult and requires a degree of self-assurance and the ability quickly to interest a buyer in the matter in hand. But it is particularly necessary that these salesmen should be able to impress the men they visit with their knowledge of what they are offering. It is also particularly the province of the salesmen to gather new names of investors, and upon their doing so conscientiously depends largely the ability of the house to increase its number of customers.

Two information files, which are of the greatest value to the bond house and essential absolutely to its success, are kept in the selling department. The first, which is often the firm rock on which success is built, is the investors' list. This list will consist of the names of those who have bought from the house, and of those who are well known as buyers of bonds from other houses. A second list will be kept of possible buyers; this is, of course, a tentative list, and names will be occasionally moved to the regular list or dropped altogether. The investors' list is a source through which considerable loss may come to the house, and it is the aim of every

house to see that letters and circulars go to possible buyers only, and that useless names be discarded as rapidly as possible. The names for the investors' list are gathered through many sources, which in their relative importance are as follows: First. Through the exertions and observation of the salesmen who in their day's work meet many people. Second. Through the tax lists and records of the probate courts. Third. Through the replies to advertisements in the newspapers and financial publications. Fourth. Through the names furnished by clients. That such a list is of great value is illustrated by an instance recently published in the daily papers of a discharged employee of a bond house who took a copy of the investors' list. In this case the bond house was willing to pay twenty-five thousand dollars for its return, although the list taken was only a duplicate.

In the well-organized bond house the investors' list will be subdivided under the direction of the manager on the lines of probable sales. From his observations and experience, the manager comes to know the inclinations and preferences of the clients. Supposing, then, that the house has seen fit to purchase an issue of municipal bonds of a city in the middle west, it is the duty of the selling manager to see that an offering of those bonds is in the hands, at the earliest possible moment, of the men who are known to buy bonds of that class. In the same way he will so direct his salesmen that they will visit first those who will be most inclined to consider the security offered.

The second list of importance kept by the selling department is the bond sales list. This list is entered under two heads, and consists, first, of a list under the heading of the bond description and shows to what investors or other houses the various bonds have been sold. This list becomes valuable in that, at maturity, it will enable the selling department to locate the holders of the securities, and in all probability to replace the investment with other bonds, and also should there, before maturity, arise an occasion when there is a demand for that particular issue, it will enable the house to locate the bonds and make bids where there will be probable results.

The list is also cross-entered under the name of each investor. The object in doing this is to enable the house to keep posted on the securities owned by each client. With this knowledge on hand

the house is able to talk more intelligently with him, and to **make** exchanges which are of mutual benefit.

### *The Financial Department*

Bond houses are provided generally with large amounts of capital, and, as a rule, are considerable borrowers of money in addition. It is the duty of the financial department to receive and pay for securities bought, to make deliveries of bonds sold, to arrange loans and to keep the general books of the business. The matters of receipts and deliveries are well regulated by custom and require no especial mention or description.

The item of loans is an important one, and one through which much money may be made or lost for the bond house. All loans are made on collateral, and the collateral offered by bond houses is the best obtainable, since it is good intrinsically, rapidly resalable and of known values. In the conduct of its business the bond house comes to know many banks and many wealthy individuals who have at certain periods of the year surplus funds. If the reputation of the house is good and the character of its securities high, these funds may often be borrowed at rates below the market for money. At all times, however, the loans of bond houses, when secured by reasonable collaterals, are looked upon with favor and command the best borrowing rate. The adjustment of loans as to time is a question of policy for the house, and the decision on these matters should come only after consideration and consultation. It is wise to keep a certain amount of loans on call, in order that the results of sales may immediately show in the interest-saved account.

If the bond house is of sufficient size and reputation, it will be advisable for it to maintain relations with one or more foreign banks, in order that loans may be made in the cheapest money market. Once the relationship is established, foreign banks will accept readily the time drafts of the bond houses; but they will demand the deposit of well-known and readily salable securities as collateral. The desirability of these connections has brought many bond houses into a regular foreign banking business, and inversely, a well-established foreign business has made a bond business adjunct desirable, so that we now see the foreign banking houses doing a large business in bonds. Some bond houses, when of sufficient reputation, borrow **funds** from their clients and others by soliciting deposits, on which

the best market rate is paid; but as this is properly a function of banking, the particular features of it will not be considered at this time.

Under the head of the financial department, it may be appropriate to call attention to the one particular in which the bond business differs from all others, except that of the dealer in commercial paper, *i. e.*, the cumulative nature of its stock on hand. In every other business where the functions of wholesaler and retailer appear, the item of interest on loans is a direct charge against selling profits, but bonds are themselves interest earners and the charge of interest becomes one of arbitrage only, depending on whether or not the bonds yield a greater interest return to the house than is paid on loans. In the average year, owing to the nature of its collateral, the bond house is able to borrow money at less than the average return of its investments, and the interest item is one of credit and a source of profit.

The keeping of the general books of the business is clerical in its nature, and requires no consideration in this paper. There are, however, many technical details, and the work should be in the hands of experienced and careful men.

The component parts of the organization of a bond house have now been considered. There are many details of the business of which no mention has been made. The transactions of syndicates and joint accounts, *et cetera*, have been omitted purposely, since their operation and management would require too much description. The effort has been made to show the skeleton structure about which the business has been built. In closing the paper, the writer wishes to say that, in his opinion, the bond house, *i. e.*, the strictly investment house, may expect to be successful if it has the following attributes, which are important in the order given:

- First. Absolute honesty.
- Second. Conservative and careful buying.
- Third. Energetic selling.
- Fourth. Well-developed system.
- Fifth. Conservative financial management.
- Sixth. Dignity.